Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

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Related Bills: See Legislative History | Telephone: 845-3627 | Introduced Date: 02-17-00

Attorney: Patrick Kusiak | Sponsor:

SUBJECT: Sales or Use Tax Paid for Agricultural Equipment Credit

SUMMARY

This bill would provide a credit equal to the sales or use tax paid or incurred during the taxable or income year for agricultural equipment (as defined).

EFFECTIVE DATE

As a tax levy, this bill would be effective immediately upon signature and would be operative for taxable or income years beginning on or after January 1, 2001, and before January 1, 2006.

LEGISLATIVE HISTORY

SB 818 (1999/2000) failed Legislature, would have extended the manufacturers' investment credit (MIC) to include activities related to the packaging, cold storage or preparing of agricultural commodities; AB 138 (1997/1998) failed Legislature, would have extended the MIC to include activities related to the packaging, cold storage or preparing of agricultural commodities; SB 94 (1997/1998) failed Legislature, would have expanded the MIC to include specified activities relating to oil and gas extraction described in Standard Industrial Classification (SIC) Codes 1311 to 1389 and activities relating to agricultural commodities described in SIC Codes 0111 to 0291, or 0724

SPECIFIC FINDINGS

Current federal and state laws provide for various tax credits designed to provide tax relief for taxpayers that incur certain expenses (e.g., child and dependent care credits) or to influence business practices and decisions.

Current federal and state laws contain a variety of different tax provisions relating to farmers. Federal law allows a credit for federal excise taxes on gasoline and special fuels used in farming (as well as certain other purposes). State law allows two credits related to farmworker housing and another for the transportation costs of agricultural products donated to a charitable organization. Neither federal nor state laws allow a credit specifically related to agricultural equipment.

Board Position:			Department Director	Date
______ S	______ NA	______ NP	Alan Hunter for GHG	3/14/00
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Current state law provides exemption from sales tax for certain items that assist an agricultural business in the production of livestock and crops. These items which constitute food for human consumption or are to be sold in the regular course of business include: feed for any form of animal life, seeds and plants, fertilizer to be applied to land, and drugs and medicines, including oxygen, that's primary purpose is to prevent or control disease of animal life, the product of which constitutes food for human consumption.

This bill would provide a credit equal to the sales or use tax paid or incurred during the taxable or income year for agricultural equipment.

This bill would define the term "agricultural equipment" as implements of husbandry, as defined by reference to Revenue and Taxation Code (R&TC) Section 411, including equipment used in forestry, dairy, cattle, pork, or poultry operations. R&TC Section 411 defines implements of husbandry to include any tool, machine, equipment, appliance, device, or apparatus used in the conduct of agricultural operations. It expressly excludes such implements intended for sale in the ordinary course of business but includes any implement of husbandry defined under the Vehicle Code. The Vehicle Code defines an "implement of husbandry" as a vehicle that is used exclusively in the conduct of agricultural operations. Such vehicles include lift carriers or similar vehicles, certain trailers or semi-trailers , spray or fertilizer applicator rigs, nurse rigs or equipment auxiliary thereto, row dusters, wagons or vans used exclusively in farming, wagons or portable houses on wheels used solely by shepherds.

Since **this bill** does not specify otherwise, the general rules in state tax law regarding credits, such as the division of credits among taxpayers who share in the expenditure subject to the credit, would apply.

Policy Considerations

A number of the items purchased and used by agricultural businesses, such as animals, seed, or fertilizer, are exempt from the state's sales tax. The author may want to consider exempting agriculture equipment from the sales and use tax rather than providing a credit equal to the sales and use tax paid for agricultural equipment, especially since many farmers report net operating losses or low net income and would not benefit from the credit.

This bill would not be limited to agricultural equipment used on farms in California, allowing the credit to taxpayers in other states who earn income from California sources and therefore have a state tax liability. In addition, since the bill does not specify that the bill is intended to provide a credit for the payment of **California** sales or use tax, the credit would be allowable for sales and use taxes paid to another state.

Other credits that are based on the sales or use tax paid for qualified property, such as the credits allowed to taxpayers within Economic Development Areas or the Manufacturers' Investment Credit, generally contain certain limitations or restrictions.

Such credits require recapture of the credit amount if the equipment is sold or disposed of within the year the credit is claimed, prohibit the basis of the subject property from being increased for depreciation purposes by the sales or use tax, and specify that if the subject property qualifies for two different credits, the taxpayer may claim only one credit. This bill does not contain similar restrictions.

There may be conflicting tax policies when a credit is provided for an expense item for which a tax benefit is already allowed in the form of a deduction. This proposed credit would have the effect of providing a double benefit for taxpayers that deduct an agricultural expense as an ordinary and necessary business expense. However, eliminating the double benefit by expressly denying the deduction or making an adjustment to reduce basis for depreciable agricultural equipment would create a state and federal difference, which is contrary to the state's general conformity policy.

Implementation Considerations

This bill would allow a credit equal to the sales and use tax paid or incurred during the taxable year for agricultural equipment. However, this bill does not limit the eligibility of the credit to the taxpayer that incurred or paid the sales and use tax; therefore, any taxpayer filing a state tax return could be interpreted to be eligible for the credit. To ensure proper interpretation, this bill should state that the credit is allowed to a “qualified taxpayer” and specifically define that term to include only those to whom the credit is intended.

Since this bill would permit unlimited credit carryover, the department would be required to retain the carryover credit on the tax forms indefinitely. Recent credits provide carryover limits because experience shows credits are typically used within eight years of being earned.

Once the implementation concerns are resolved, implementing this bill would not significantly impact the department’s programs and operations.

FISCAL IMPACT

Departmental Costs

This bill would not significantly impact the department’s costs.

Tax Revenue Estimate

The revenue impact of this measure, under the assumptions discussed below, is estimated to be as follows:

Revenue Impact of the Proposal Income/Taxable Years Beginning On or After 1/1/2001 Enactment Assumed After June 30, 2000 **(In Millions)**			
	2000-1	2001-2	2002-3
Revenue Impact	($2)	($10)	($15)

It is assumed that qualified equipment would have to be placed in service in California. This analysis does not account for changes in employment, personal income, or gross state product that could result from this measure.

Tax Revenue Discussion

The estimates are based on the following information. The average value of qualified equipment purchased was calculated using the data on the values of machinery and equipment on California farms from the 1992 and 1997 censuses (about $5 billion for 1997 and $4 billion for 1992). It is projected the total value of new and used equipment placed in service in California for 2000 will be $250 million. Estimates took into account the fact many farmers have operating losses or low net incomes for the year. An average sales/use tax rate of 7.25% was used for the calculations.

BOARD POSITION

Pending.